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C O N F I D E N T I A L SECTION 01 OF 02 RIGA 000238

SIPDIS

TREASURY FOR DAVID WRIGHT

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TAGS: [ECON](#) [PGOV](#) [SOCI](#) [LG](#)
SUBJECT: PRESIDENT PUSHES GOVERNMENT TO GET SERIOUS ON
BUDGET

Classified By: Charge d'Affaires Tamir Waser for Reasons 1.4 (b) and (d)
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¶1. (C) Summary. At the request of President Zatlers, the Cabinet held a extraordinary session on April 24 to discuss budget and government reform issues, specifically focusing on overhauling Latvia's health and education services. This meeting is being followed by a second extraordinary session on April 30, where the government may start making decisions on the size of additional budget cuts to each ministry. (Comment: The reform plans agreed in principle on the 24th and the cuts being considered on the 30th are dramatic, but there is still a way to go before they are finalized. That the President is using his authority to help drive the process is indicative of the political challenges involved. These steps are essential prerequisites before an IMF assessment mission in early May. If the Fund views these steps as genuine reforms, Latvia may get flexibility on its deficit target for 2009. If not, the crunch will be even tighter.) End summary.

¶2. (C) Head of the President's Chancery, Edgars Rinkevics, told us that President Zatlers had called on the government to begin serious discussions on how Latvia would meet its commitments to international lenders, and to do so in a transparent manner, informing the public of its decisions and reasoning. Rinkevics said that the April 24 extraordinary Cabinet meeting was held in response to this request, and though the meeting was closed-door, he said the President was pleased at the results of the session. According to sources in the MFA and Finance Ministry, the meeting on the 24th focused on large-scale reforms to Latvia's health and education systems, and on making government administration more effective. Reforms to education and health services had been suggested by the World Bank before last year's economic downturn, but implementation of the World Bank recommendations was never carried out. Reform of the two systems is now a condition of the IMF and European Commission-led financial assistance package that Latvia agreed to in December 2008, and the World Bank recommendations are being used as guidelines.

¶3. (C) According to the Director of the Finance Ministry's Budget Department, Ilonda Stepanova, reforms suggested in the April 24 session were to centralize both medical and educational facilities (closing underutilized rural schools and small medical facilities), reduce the number of non-service providing agencies in the medical administration sector, move to more out-patient medical procedures in lieu of overnight hospital stays, and look at merging various vocational schools and educational programs. She said that no final decisions were taken, and that because of the shared nature of education financing between the central and local governments, school closures would have to be agreed to at both the local and national levels. The PM's economic advisor, Gints Freimanis, stated that optimization in schools may cost the jobs of 2,000-4,000 teachers, and that in the

health sector, 24 hospitals may need to be closed.

¶4. (C) The second Cabinet session on April 30 is to consider specific budgets for the individual ministries. The PM had earlier tasked ministries to prepare budget scenarios for cuts of 20%, 30% and 40%. Stepanova said that the Cabinet would likely start choosing which options the ministries need to implement, though she said most would be asked to implement their 40% budget cut scenarios. This assessment matches with what we had earlier heard from MFA U/S Maija Manika. Specific to her ministry, Manika said that if faced with a 40% funding cut, the MFA could close up to two-thirds of its representations overseas.

¶5. (C) The government's continued search for cost savings is necessitated by its need to meet the guidelines set by international lenders - namely that this year's deficit not exceed 5% of GDP. Latvia's largest newspaper, Diena, reported on the morning of April 30 that Latvia had received permission to run a 7% of GDP budget deficit, but that claim was quickly refuted by Finance Minister Repse.

¶6. (C) Comment: The government has been urged by both IMF and U.S. Treasury Department representatives recently to prioritize government spending items and not continue looking for across-the-board cuts to ministries. The current budget process, with each ministry preparing various funding scenarios, appears to support prioritization of government services. The extraordinary Cabinet sessions are a welcome sign that the government is starting make progress in implementing uncomfortable reforms, but having the President pushing the agenda rather than the PM underscores the

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political challenges of such cuts, especially in the run up to June 6 local and European Parliament elections.
WASER